

Message Text

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ACTION EUR-08

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R 022341Z MAR 77 CORRECTED COPY FOR MRN
FM AMEMBASSY OTTAWA
TO SECSTATE WASHDC 2641
INFO AMCONSUL MONTREAL
ALL OTHER CONGENS IN CANANDA (BY POUCH)

C O N F I D E N T I A L SECTION 1 OF 2 OTTAWA 01217

LIMDIS

C O R R E C T E D C O P Y FOR MRN UPDATE 01217 VICE 00002

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DEPARTMENT PASS NSC, CEA, TREASURY, FRB

E.O. 11652: GDS
TAGS: EFIN, CA
SUBJECT: FINANCIAL CONDITIONS IN QUEBEC

1. SUMMARY: PRELIMINARY SURVEY WITH ASSISTANCE OF
CONGENS QUEBEC AND MONTREAL INDICATES QUEBEC PROVINCE
AND ITS AGENCIES WILL NOT ENCOUNTER UNSURMOUNTABLE
PROBLEMS IN MEETING FINANCING REQUIREMENTS THIS YEAR AND
IN FORESEEABLE FUTURE. COSTS OF BORROWING HAVE INCREASED
WITH POLITICAL UNCERTAINTY. ECONOMIC OUTLOOK FOR PROVINCE
THIS YEAR IS DISMAL. SLOW REAL GROWTH AND RISING
UNEMPLOYMENT EXPECTED ARE DUE IN LARGE PART TO LOWER
LEVELS OF NEW PRIVATE INVESTMENT FROM OUTSIDE PROVINCE
FOR OTHER THAN ONGOING PROJECTS. DESPITE LITTLE DETAILED
DATA AND ANALYSIS OF ECONOMIC AND FINANCIAL CONDITIONS,
EARNEST BUREAUCRATS IN QUEBEC CITY ARE RIDING HIGH,
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CONFIDENT SEPARATION IS IN BEST ECONOMIC INTERESTS OF
THE PROVINCE. MONTREAL FINANCIAL COMMUNITY IS DEFENSIVE
BUT FEELS LARGELY HELPLESS FOR NOW IN COMBATTING
SEPARATISM. END SUMMARY.

2. WITH ASSISTANCE OF CONGENS QUEBEC AND MONTREAL,
EMBASSY HAS RECENTLY INITIATED STUDY OF FINANCIAL

CONDITIONS IN QUEBEC PROVINCE, PARTICULARLY SOURCES AND USES OF FUNDS FOR PROVINCIAL FINANCING AND FEDERAL-PROVINCIAL FINANCIAL RELATIONS. DETAILED ANALYSES WILL BE REPORTED IN DUE COURSE. THIS CABLE SUMMARIZES INITIAL IMPRESSIONS BASED ON LONGER MEMO WHICH IS BEING POUCHED TO INTERESTED END-USERS.

3. ECONOMIC OUTLOOK FOR PROVINCE THIS YEAR IS BLEAK. ROUGH ESTIMATES OF REAL GROSS PROVINCIAL PRODUCT (GPP) GROWTH RANGE FROM 2.1 TO 2.8 PERCENT. UNEMPLOYMENT EXPECTED TO RISE FROM AVERAGE 1976 RATE OF JUST UNDER NINE PERCENT TO BETWEEN 10 AND 11 PERCENT IN 1977. CONSUMPTION AND GOVERNMENT SPENDING ARE EXPECTED TO BE WEAK AND IMPACT OF PRIVATE INVESTMENT ON GPP MAY BE NEGATIVE. LITTLE NEW INVESTMENT FROM ABROAD IS EXPECTED EXCEPT FOR ONGOING PROJECTS UNTIL POLITICAL SITUATION CLARIFIES.

4. FEW DETAILS OR CURRENT DATA ARE AVAILABLE ON PROVINCIAL TRADE AND INVESTMENT. ONE UNPUBLISHED STUDY INDICATES ABOUT HALF OF 1973 BUSINESS FIXED INVESTMENT ORIGINATED FROM OUTSIDE CANADA. MERCHANDISE TRADE WITH REST OF CANADA AND WORLD ACCOUNTS FOR ABOUT ONE-THIRD OF GPP. EXPORTS ABROAD, MOSTLY TO THE U.S., ACCOUNT FOR ABOUT 15 PERCENT OF GPP.

5. PROVINCIAL BUDGET FOR FISCAL YEAR BEGINNING APRIL AGAIN EXPECTED TO BE IN DEFICIT BY MORE THAN \$800 MILLION. MAIN CHANNEL OF PRIVATE SAVINGS FOR FINANCING CONFIDENTIAL

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DEFICIT IS PROVINCIAL PENSION FUND (CAISSE DE DEPOT). ASSETS IN 1975 GREW \$800 MILLION TO \$4.3 BILLION, ABOUT HALF OF WHICH IS HELD IN BONDS OF PROVINCE AND AGENCIES. CAISSE REPORTEDLY INTERVENED AFTER NOVEMBER ELECTION BY SELLING FEDERAL BONDS TO BANK OF CANADA AND BUYING PROVINCIAL BONDS TO RESIST THEIR PRICE DECLINE.

6. LEVELS OF PER CAPITA PROVINCIAL DEBT ARE THE LOWEST IN CANADA AND PER CAPITA INCOME THROUGH 1975 WAS INCREASING FASTER THAN PER CAPITA PROVINCIAL DEBT. NEITHER PROVINCIAL OFFICIALS NOR MONTREAL UNDERWRITERS EXPECT QUEBEC WILL FACE CASH CRUNCH THIS YEAR DUE TO LACK OF NECESSARY ACCESS TO FOREIGN CAPITAL MARKETS. ALL BELIEVED HYDRO-QUEBEC COULD CONTINUE ACCESS TO NEW YORK LATER THIS YEAR WHILE PROVINCE WOULD BE ABLE TO CONTINUE TO BORROW AS NEEDED OUTSIDE THE PROVINCE FROM EUROPE AND ELSEWHERE.

7. THERE IS EVIDENCE QUEBEC HAS RUN A CURRENT ACCOUNT SURPLUS WITH THE REST OF THE WORLD IN MOST YEARS SINCE

THE EARLY 1960'S WHILE THE REST OF CANADA WAS LARGELY IN DEFICIT. THERE ALSO APPEARS TO HAVE BEEN SOME NET CAPITAL OUTFLOW TO THE REST OF CANADA VIA PREMIUMS PAID IN BY QUEBEC RESIDENTS AND INVESTED BY INSURANCE COMPANIES ELSEWHERE.

8. SINCERE, SELF-CONFIDENT OFFICIALS IN QUEBEC CITY OFTEN SEEM TO OPERATE ON BASIS THEIR OWN SUBJECTIVE FEEL RATHER THAN HARD DATA OR ANALYSIS OF ECONOMIC OR FINANCIAL ISSUES. THEY ASSERT QUEBEC MUST HAVE ITS OWN SEAT IN GATT AND DEGREE OF MONETARY INDEPENDENCE, EVEN WITHIN CUSTOMS AND MONETARY UNION WITH CANADA. INTERDEPENDENCE WITH ONTARIO CITED AS GROUNDS FOR BELIEVING

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C O N F I D E N T I A L SECTION 2 OF 2 OTTAWA 01217

C O R R E C T E D C O P Y FOR MRN UPDATE 01217 VICE 00002

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ADEQUATE COMMERCIAL RELATIONS CAN BE MAINTAINED WITH REST OF CANADA AFTER SEPARATION.

9. POLICY INITIATIVE NOW LIES WITH HIGHLY MOTIVATED FRANCOPHONE OFFICIALS IN QUEBEC CITY. BILINGUAL FINANCIAL COMMUNITY IN MONTREAL SEEMS DEMORALIZED AND HELPLESS FOR NOW IN COMBATTING SEPARATISM. ALTHOUGH IN THE END ECONOMIC ARGUMENTS -- EVEN BASED ON MORE PRECISE DATA THAN NOW AVAILABLE -- ARE UNLIKELY TO BE DECISIVE IN SEPARATIST/FEDERALIST DISPUTE, POOR ECONOMIC PERFORMANCE EXPECTED FOR AT LEAST THE NEXT YEAR WILL PROBABLY EXACERBATE POLITICAL TENSIONS IN THE PROVINCE. ENDERS

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